TESTIMONY OF M. ELLIOTT BATSON, JR.

FOR

DUKE POWER

PSCSC DOCKET NO. 2004-003-E

Q. PLEASE STATE YOUR NAME, ADDRESS AND POSITION WITH DUKE POWER.

A. My name is Elliott Batson and my business address is 526 South Church Street, Charlotte, North Carolina. I am Manager, Coal and Bulk Material Procurement of Duke Power, a division of Duke Energy Corporation ("Duke Power" or "the Company).

Q. STATE BRIEFLY YOUR EDUCATION, BUSINESS BACKGROUND AND PROFESSIONAL AFFILIATIONS.

A. I am a 1985 graduate of the University of South Carolina with a Bachelor of Science in Business Administration. I have been employed with Duke Power since 1986 and have worked in the Fossil Fuel Procurement area since 1990. I am a member of the North Carolina Coal Institute.

Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING?

A. The purpose of my testimony is to furnish information relating to our fossil fuel purchasing practices and costs for the period April 2003 through March 2004 and describe any anticipated changes forthcoming in the projected period.

Q. YOUR TESTIMONY INCLUDES 2 EXHIBITS. WERE THESE EXHIBITS PREPARED BY YOU OR AT YOUR DIRECTION AND UNDER YOUR SUPERVISION?

A. Yes. Each of these exhibits was prepared at my direction and under my supervision.

Q. CAN YOU PROVIDE A SUMMARY OF DUKE POWER'S FOSSIL FUEL PROCUREMENT PRACTICES?

A. Yes. The Company continues to follow the same procurement practices it has historically followed, and a summary of those practices is as follows:

1. Estimating Fuel Requirements. Fuel requirements are estimated monthly and annually based on data input from several functions, including load forecasting, and reflect system planning considerations, as well as nuclear and fossil capacity factors.

2. Establish Inventory Requirements. Monthly and annual fuel inventory requirements for each station and the system are determined after considering the Company's purchasing and production requirements.

3. Monitoring On-going Fuel Requirements. On a monthly and annual basis, reviews are made of existing contracts and projected consumption to determine the need for additional spot or contract supplies.

4. Develop Qualified Supplier Lists. A list of qualified suppliers is maintained along with detailed historical records of their performance and capabilities as to quantity, quality, loading capabilities, etc. Invitations to bid are distributed to all qualified suppliers to cover additional or future contract needs.

5. Bid Evaluation. Contracts are awarded after a complete evaluation cycle, including, if necessary, an on-site visit to the source to determine the capabilities of the suppliers.

6. Spot Purchases. To supplement our fuel supply, short term spot market offers are received on a monthly basis and purchases are made in accordance with needs.

7. Expediting of Purchases. All orders are expedited (monitored) closely as to performance against schedule quantity, quality, and proper bills of lading, etc.

8. On-going Quality Control. The Company samples and analyzes coal received at each station. These analyses are monitored closely against contract specifications and serve as the basis for final price determinations. Coal is weighed at each station to verify freight charges assessed by the railroads.

Q. WHAT IS SHOWN ON BATSON EXHIBIT 1?

A. Batson Exhibit 1 is a statistical summary for each fossil fuel category for the period April 2003 through March 2004. The Exhibit includes the quantities consumed, quantities purchased, and the 12-month weighted average purchase price for each fuel. Due to the different components which make up the total cost of coal, coal statistics are further broken down to show the average freight on board (f.o.b.) mine cost, the transportation cost, and the delivered cost per million British Thermal Units (BTUs).

The average delivered cost per ton of coal increased from $40.47 for the twelve months ended March 31, 2003 to $44.32 for the twelve months ended March 31, 2004. The increase is due to higher coal prices in the short term spot market in 2003 and higher contract prices for coal purchased under contracts resulting from a spring 2003 Request for Proposals (RFP). Duke Power benefited from favorably priced coal contracts negotiated in previous years, which resulted in significantly lower average coal mine costs in 2003 as compared to prevailing market prices.

Average oil prices decreased almost $0.02 per gallon when compared to the previous 12-month period ending March 2003. Average natural gas prices increased 42% to $7.84/million cubic feet (mcf) when compared to the previous 12-month period ending March 2003. The increase in natural gas prices is primarily due to low storage levels (or supply of gas) in 2003 caused by the colder 2002-2003 winter weather and resulting demands on the supply market.

Q. WHAT IS SHOWN ON BATSON EXHIBIT 2?

A. This exhibit shows the Company's inventories for coal and oil at the beginning and end of this reporting period.

Coal inventories decreased from 1,921,999 tons as of March 2003 to 1,575,521 tons as of March 2004. This reduction is due to several factors including strong winter coal burns and tight market conditions for buying coal. Duke expects to maintain appropriate inventory to support summer and subsequent consumption.

Oil inventories increased from the previous period as purchases were made to fill Duke Power's oil tanks to greater capacity in 2004, particularly the inventory at Mill Creek.

Q. WHAT CHANGES DO YOU SEE IN THE COMPANY'S FOSSIL FUEL COSTS DURING THE FORECAST PERIOD?

A. As Duke Power's existing coal contracts expire, they will be replaced in today's higher priced market. These contract purchases will be competitively bid in accordance with Duke Power's fuel purchasing practices described earlier in my testimony. Current market prices based on a February 2004 RFP illustrate the rising coal costs in the current market and indicate contract mine prices of $42 to $52 per ton. Coal prices have increased significantly in the last year primarily due to declining coal production in Central Appalachia, changing export market conditions for Central Appalachian coal, and increasing operating costs. Central Appalachian coal production declined 8% from 2002 to 2003 because of more stringent environmental regulations and permitting requirements, and the necessity of mining in more difficult coal seams and conditions. Increased demand and reduced coal production in Asia have resulted in increasing coal exports from Central Appalachia to foreign markets. In addition, operating costs for coal producers are increasing due to higher petroleum costs, higher labor costs due to a shrinking skilled work force and tighter truck-hauling restrictions. As a result, the company's cost of coal will be increasing in 2004 compared to 2003.

Q. WHAT WERE THE COMPANY'S COAL TRANSPORTATION COSTS FOR THE PERIOD?

A. Coal transportation or freight costs for the calendar year 2003 were $255 million, or $15.17 per ton compared to $226 million, or $15.22 per ton in 2002.

Q. IN DUKE POWER'S LAST FUEL ADJUSTMENT PROCEEDING IN DOCKET NO. 2003-3-E, YOU TESTIFIED TO INCREASED COAL TRANSPORTATION COSTS AS A RESULT OF PENDING LITIGATION BEFORE THE SURFACE TRANSPORTATION BOARD ("STB"). PLEASE PROVIDE THE STATUS OF THAT LITIGATION.

A. In order to contest a significant increase in the rates Norfolk Southern Railway Company and CSX Transportation charged the Company for freight charges beginning January 1, 2002, Duke Power filed complaints with the Surface Transportation Board.

On November 5, 2003, the STB issued an Order in the Norfolk Southern case that denied Duke Power's complaint and concluded that the tariff rates the Company has been paying since January 1, 2002, are not unreasonable. In response, Duke Power filed a petition for correction of technical errors, and the STB revised its decision on February 3, 2004, finding that Duke Power is entitled to some rate relief in the Norfolk Southern case. However, the STB stayed its November 5, 2003 decision because both Duke Power and Norfolk Southern indicated further petitions for reconsideration would be filed. Both Duke Power and Norfolk Southern filed petitions for reconsideration on February 23, 2004. On March 15, 2004 each party filed a reply to other party's petition for reconsideration.

On February 3, 2004, the STB issued an order in the CSX Transportation case that denied Duke Power's complaint and concluded that the tariff rates the Company has been paying since January 1, 2002, are not unreasonable. Duke Power filed a petition for correction of technical errors on March 16, 2004, and a petition for reconsideration on March 25, 2004. CSX filed a response to Duke Power's petition for correction of technical errors on April 5, 2004. On April 14, 2004, each party filed a reply to the other party's petition for reconsideration.

The Company does not expect any significant changes in transportation costs in 2004, unless the outcome of the STB rate cases is modified by the STB upon reconsideration.

Q. MR. BATSON, DOES THAT CONCLUDE YOUR TESTIMONY?

A. Yes, it does.